

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 98-0384
STATE GROSS RETAIL TAX
For Years 1995, 1996, and 1997**

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ISSUES

I. Sales Tax on the Lease of Tangible Personal Property: Leased Equipment

Authority: IC 6-2.5-4-10(a); 45 IAC 2.2-4-27(a); 45 IAC 2.2-4-27(c).

Taxpayer protests the assessment of sales tax on leased equipment because taxpayer considers lease transactions as services and not transfers of tangible personal property.

II. Sales Tax on Transactions Involving Tangible Personal Property and Services: Tax on Services

Authority: IC 6-2.5-1-1; IC 6-2.5-1-2(b); IC 6-2.5-2-1; IC 6-2.5-4-1(b); 45 IAC 2.2-1-1(a); 45 IAC 2.2-4-2(a)(3).

Taxpayer protests the assessment of sales taxes on transactions which include the provision of both labor and tangible personal property.

III. Request for Abatement of 10% Negligence Penalty: Penalty Abatement

Authority: IC 6-8.1-10-2.1; IC 6-8.1-10-2.1(d); 45 IAC 15-11-2(c).

Taxpayer protests the assessment of the 10% negligence penalty and requests that the penalty be abated.

IV. Request for Abatement of Interest: Interest Abatement

Authority: IC 6-8.1-10-1; IC 6-8.1-10-1(a).

Taxpayer protests the imposition of interest on assessed taxes and requests that the interest that has accumulated on those assessed taxes be abated.

Statement of Facts

Taxpayer's business activity consists of the sale, installation, and maintenance of home and commercial audio and video systems. Taxpayer sells, installs, and services electronic security systems and fire alarm systems. Taxpayer also provides alarm-monitoring services. Under some circumstances, taxpayer leases the equipment.

I. Sales Tax on the Lease of Tangible Personal Property: Leased Equipment

Taxpayer argues that sales tax was improperly assessed on transactions involving leased equipment. Taxpayer asserts that these transactions did not involve the transfer of tangible personal property but were service transactions. Taxpayer avers that the lease agreements did not provide for the purchase of the equipment but that taxpayer, at all times, retained title of the equipment.

Under IC 6-2.5-4-10(a), a person who rents or leases tangible personal property to another engages in a taxable retail transaction. Therefore, that retail transaction is subject to sales tax.

Under 45 IAC 2.2-4-27(a), gross receipts resulting from the lease of tangible personal property are taxable. The lease of tangible personal property is treated the same as the sale of that property for the purpose of determining the gross retail tax. Exemptions are provided for lease transactions which would have been exempt in an equivalent sales transaction.

The lessor, under 45 IAC 2.2-4-27(c), acts as an agent of the state and is responsible for the collection and remittance of the gross retail tax. The lessee is liable for the tax on the lease transaction, but the lessor must collect the tax and remit it to the state.

FINDING

Taxpayer's protest is respectfully denied.

II. Sales Tax on Transactions Involving Sales of Tangible Personal Property and Services: Tax on Services

Taxpayer protests the assessment of the gross retail tax on those portions of transactions related to the provision of labor. Before entering into these transactions, typically for the sale and installation of alarm, video, or audio systems, taxpayer quoted customer a lump sum price. Once the customer accepted the price and the project began, taxpayer billed customer twice based upon the stage of completion the project had reached.

The first bill, called the “rough-in” bill, was the charge for labor expended in preparatory work at the installation site. The “rough-in” bill also included taxpayer’s charge for the design work.

The second bill was the “finish” bill which included the cost of materials, equipment, and remaining labor costs. The audit concluded that the taxpayer was a retail merchant in regard to the sale of these systems and that all elements of consideration were subject to the sales tax.

Under IC 6-2.5-2-1, the state imposes a state gross retail (sales) tax on retail transactions made in Indiana. A retail transaction, the prerequisite to the imposition of the tax, is the transfer, in the ordinary course of business, of tangible personal property for consideration. IC 6-2.5-4-1(b). Therefore, absent the transfer of tangible personal property, the transfer of services alone is not subject to the state gross retail tax.

However, the transfer of services is taxed if it is part of a retail “unitary transaction.” IC 6-2.5-1-2(b). A retail “unitary transaction” is one in which items of personal property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC 6-2.5-1-1. A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. 45 IAC 2.2-1-1(a).

Taxpayer issues two bills for each installation transaction. The first of the two bills, the “rough-in” bill, represents taxpayer’s charge for the cost of his preliminary, on-site labor and a charge for taxpayer’s associated design work. Income derived from this “rough-in” bill is not subject to the gross retail tax under IC 6-2.5-2-1 because, absent a co-extensive transfer of tangible personal property, it is not a retail transaction.

Taxpayer’s second bill, its “finish” bill, represents a unitary transaction under IC 6-2.5-1-1 because it represents the cost of personal property (audio, video, security equipment) together with labor costs associated with the completion of customer’s installation project. Because taxpayer did not separately state these services on the “finish” invoices, all income derived from taxpayer’s “finish” bills is subject to the gross retail tax. Further, taxpayer does not contend that the cost of the personal property represented in its final “finish” bill is inconsequential (not exceeding 10% compared to the service charge) and that, as a result, taxpayer’s “finish” bill is exempt from the tax under 45 IAC 2.2-4-2(a)(3).

FINDING

Taxpayer’s protest is sustained in part and denied in part.

To the extent that taxpayer’s “rough-in” bills represent exclusively the costs of taxpayer’s preliminary on-site labor and design charges, those bills are exempt from the gross retail tax. Taxpayer’s “finish” bills, representing an undifferentiated unitary transfer of tangible

personal property and taxpayer's final labor charges, are subject to the gross retail tax. Audit is requested to conduct a supplementary audit for the purpose of determining taxpayer's gross retail tax liability based upon taxpayer's "finish" bills.

III. Request for Abatement of 10% Negligence Penalty: Penalty Abatement

Taxpayer protests the imposition of the 10% negligence penalty and requests that the penalty, assessed pursuant to IC 6-8.1-10-2.1, be abated. Under IC 6-8.1-10-2.1(d), the Department is empowered to waive the 10% negligence penalty if taxpayer can establish that his failure to pay the deficiency was due to reasonable cause and not due to willful neglect. Under 45 IAC 15-11-2(c), in order to establish reasonable cause, the taxpayer must demonstrate that he exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed. Ignorance of the listed tax laws, rules, and/or regulations is treated as negligence.

Factors which may be considered to determine reasonable cause include the nature of the tax involved, judicial precedents set by Indiana courts, judicial precedents established in jurisdictions outside Indiana, published department instructions, information bulletins, letters of findings, rulings, and letters of advice. 45 IAC 15-11-2(c).

Taxpayer argues that he has never fraudulently withheld trust taxes nor did he deliberately attempt to avoid collecting sales taxes. Taxpayer states that since the audit clarified taxpayer's responsibility for collecting and paying sales taxes, taxpayer has begun to itemize material on sales invoices, begun collecting sales tax on both leased equipment and transactions associated with new construction.

Taxpayer's effort to comply with his tax responsibilities is commendable. However, taxpayer has failed to meet his burden of demonstrating that reasonable cause existed for his past failure to comply with those tax responsibilities.

FINDING

Taxpayer's protest and request for abatement is respectfully denied.

IV. Request for Abatement of Interest: Interest Abatement

Taxpayer protests the imposition of interest on assessed taxes and requests that the interest that has accumulated on those assessed taxes be abated. Under IC 6-8.1-10-1(a), if a person incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

The Department has no discretion regarding the imposition of interest. Under IC 6-8.1-10-1, interest is not abated for any reason.

FINDING

Taxpayer's protest and request for abatement is respectfully denied.